HOVNANIAN ENTERPRISES INC
Form 10-Q
June 09, 2015
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UNITED STATES

SECURITIES AND EXCHANGE COMMISSION

WASHINGTON, D.C. 20549

FORM 10-Q

(Mark One)

[X] Quarterly report pursuant to Section 13 or 15(d) of the Securities Exchange Act of 1934

For the quarterly period ended APRIL 30, 2015

OR

[ ] Transition report pursuant to Section 13 or 15(d) of the Securities Exchange Act of 1934

Commission file number 1-8551

Hovnanian Enterprises, Inc. (Exact Name of Registrant as Specified in Its Charter)

Delaware (State or Other Jurisdiction of Incorporation or Organization)

22-1851059 (I.R.S. Employer Identification No.)

110 West Front Street, P.O. Box 500, Red Bank, NJ 07701 (Address of Principal Executive Offices)

732-747-7800 (Registrant's Telephone Number, Including Area Code)

N/A (Former Name, Former Address and Former Fiscal Year, if Changed Since Last Report)

Indicate by check mark whether the registrant: (1) has filed all reports required to be filed by Section 13 or 15(d) of the Securities Exchange Act of 1934 during the preceding 12 months (or for such shorter period that the registrant was required to file such reports), and (2) has been subject to such filing requirements for the past 90 days.

Yes [X] No [ ]

Indicate by check mark whether the registrant has submitted electronically and posted on its corporate web site, if any, every Interactive Data File required to be submitted and posted pursuant to Rule 405 of Regulation S-T (§ 232.405 of this chapter) during the preceding 12 months (or for such shorter period that the registrant was required to submit and post such files). Yes [X] No [ ]

Indicate by check mark whether the registrant is a large accelerated filer, an accelerated filer, a non-accelerated filer, or a smaller reporting company. See the definitions of “large accelerated filer,” “accelerated filer” and “smaller reporting company” in Rule 12b-2 of the Exchange Act.

Large Accelerated Filer [ ] Accelerated Filer [X]

Non-Accelerated Filer [ ] (Do not check if smaller reporting company) Smaller Reporting Company [ ]

Indicate by check mark whether the registrant is a shell company (as defined in Rule 12b-2 of the Exchange Act). Yes [ ] No [X]

Indicate the number of shares outstanding of each of the issuer's classes of common stock, as of the latest practicable date. 131,435,644 shares of Class A Common Stock and 14,983,719 shares of Class B Common Stock were outstanding as of June 4, 2015.

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HOVNANIAN ENTERPRISES, INC.

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HOVNANIAN ENTERPRISES, INC. AND SUBSIDIARIES

CONDENSED CONSOLIDATED BALANCE SHEETS

(In Thousands)

	April 30, 2015 (Unaudited)	October 31, 2014 (1)
ASSETS		
Homebuilding:		
Cash and cash equivalents	$256,866	$255,117
Restricted cash and cash equivalents	9,623	13,086
Inventories:		
Sold and unsold homes and lots under development	1,227,692	961,994
Land and land options held for future development or sale	210,259	273,463
Consolidated inventory not owned:		
Specific performance options	1,734	3,479
Other options	99,072	105,374
Total consolidated inventory not owned	100,806	108,853
Total inventories	1,538,757	1,344,310
Investments in and advances to unconsolidated joint ventures	70,550	63,883
Receivables, deposits and notes, net	85,810	92,546
Property, plant and equipment, net	46,414	46,744
Prepaid expenses and other assets	81,085	69,358
Total homebuilding	2,089,105	1,885,044
Financial services:		
Cash and cash equivalents	4,706	6,781
Restricted cash and cash equivalents	13,980	16,236
Mortgage loans held for sale at fair value	106,452	95,338
Other assets	2,163	1,988
Total financial services	127,301	120,343
Income taxes receivable – including net deferred tax benefits	300,588	284,543
Total assets	$2,516,994	$2,289,930

(1) Derived from the audited balance sheet as of October 31, 2014.

See notes to condensed consolidated financial statements (unaudited).

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HOVNANIAN ENTERPRISES, INC. AND SUBSIDIARIES

CONDENSED CONSOLIDATED BALANCE SHEETS

(In Thousands Except Share and Per Share Amounts)

	April 30, 2015 (Unaudited)	October 31, 2014 (1)
LIABILITIES AND EQUITY		
Homebuilding:		
Nonrecourse mortgages	$118,904	$103,908
Accounts payable and other liabilities	342,762	370,876
Customers' deposits	41,431	34,969
Nonrecourse mortgages secured by operating properties	16,076	16,619
Liabilities from inventory not owned	91,040	92,381
Total homebuilding	610,213	618,753
Financial services:		
Accounts payable and other liabilities	21,831	22,278
Mortgage warehouse lines of credit	82,966	76,919
Total financial services	104,797	99,197
Notes payable:		
Senior secured notes, net of discount	980,629	979,935
Senior notes, net of discount	840,851	590,472
Senior amortizing notes	14,987	17,049
Senior exchangeable notes	71,913	70,101
Accrued interest	39,938	32,222
Total notes payable	1,948,318	1,689,779
Total liabilities	2,663,328	2,407,729
Stockholders' equity deficit:		
Preferred stock, $0.01 par value - authorized 100,000 shares; issued and outstanding 5,600 shares with a liquidation preference of $140,000 at April 30, 2015 and at October 31, 2014	135,299	135,299
Common stock, Class A, $0.01 par value – authorized 400,000,000 shares; issued 143,196,407 shares at April 30, 2015 and 142,836,563 shares at October 31, 2014 (including 11,760,763 shares at April 30, 2015 and October 31, 2014 held in Treasury)	1,432	1,428
Common stock, Class B, $0.01 par value (convertible to Class A at time of sale) – authorized 60,000,000 shares; issued 15,675,467 shares at April 30, 2015 and 15,497,543 shares at October 31, 2014 (including 691,748 shares at April 30, 2015 and October 31,	157	155

2014 held in Treasury)		
Paid in capital – common stock	703,337	697,943
Accumulated deficit	(871,199)	(837,264)
Treasury stock – at cost	(115,360)	(115,360)
Total stockholders' equity deficit	(146,334)	(117,799)
Total liabilities and equity	$2,516,994	$2,289,930

(1) Derived from the audited balance sheet as of October 31, 2014.

See notes to condensed consolidated financial statements (unaudited).

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HOVNANIAN ENTERPRISES, INC. AND SUBSIDIARIES

CONDENSED CONSOLIDATED STATEMENTS OF OPERATIONS

(In Thousands Except Per Share Data)

(Unaudited)

	Three Months Ended April 30,		Six Months Ended April 30,	
	2015	2014	2015	2014
Revenues:				
Homebuilding:				
Sale of homes	$455,172	$438,302	$888,643	$793,483
Land sales and other revenues	1,320	2,215	2,441	2,988
Total homebuilding	456,492	440,517	891,084	796,471
Financial services	12,457	9,412	23,579	17,506
Total revenues	468,949	449,929	914,663	813,977
Expenses:				
Homebuilding:				
Cost of sales, excluding interest	382,139	350,433	736,951	639,320
Cost of sales interest	12,013	12,407	23,331	21,897
Inventory impairment loss and land option write-offs	4,311	522	6,541	1,186
Total cost of sales	398,463	363,362	766,823	662,403
Selling, general and administrative	52,614	47,806	100,260	91,768
Total homebuilding expenses	451,077	411,168	867,083	754,171
Financial services	7,508	6,707	14,825	13,379
Corporate general and administrative	16,493	14,641	33,401	31,033
Other interest	23,030	23,472	48,101	46,805
Other operations	1,788	1,151	3,332	2,260
Total expenses	499,896	457,139	966,742	847,648
Loss on extinguishment of debt	-	(1,155)	-	(1,155)
Income from unconsolidated joint ventures	1,466	1,067	2,918	3,638
Loss before income taxes	(29,481)	(7,298)	(49,161)	(31,188)
State and federal income tax (benefit) provision:				
State	(414)	604	2,718	1,237
Federal	(9,508)	-	(17,944)	-
Total income taxes	(9,922)	604	(15,226)	1,237
Net loss	$(19,559)	$(7,902)	$(33,935)	$(32,425)
Per share data:				
Basic:				
Loss per common share	$(0.13)	$(0.05)	$(0.23)	$(0.22)

Weighted-average number of common shares outstanding	146,946	146,325	146,762	146,151
Assuming dilution:				
Loss per common share	$(0.13)	$(0.05)	$(0.23)	$(0.22)
Weighted-average number of common shares outstanding	146,946	146,325	146,762	146,151

See notes to condensed consolidated financial statements (unaudited).

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HOVNANIAN ENTERPRISES, INC. AND SUBSIDIARIES

CONDENSED CONSOLIDATED STATEMENT OF EQUITY

(In Thousands Except Share Amounts)

(Unaudited)

	A Common Stock Shares Issued and Outstanding	Amount	B Common Stock Shares Issued and Outstanding	Amount	Preferred Stock Shares Issued and Outstanding	Amount	Paid-In Capital	Accumulated Deficit	Treasury Stock
Balance, October 31, 2014	131,075,800	$1,428	14,805,795	$155	5,600	$135,299	$697,943	$(837,264)	$(115,36(
Stock options, amortization and issuances	18,125						1,473		
Restricted stock amortization, issuances and forfeitures	341,619	4	178,024	2			3,921		
Conversion of Class B to Class A Common Stock	100		(100)						
Net loss								(33,935)	
Balance, April 30, 2015	131,435,644	$1,432	14,983,719	$157	5,600	$135,299	$703,337	$(871,199)	$(115,36(

See notes to condensed consolidated financial statements (unaudited).

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HOVNANIAN ENTERPRISES, INC. AND SUBSIDIARIES

CONDENSED CONSOLIDATED STATEMENTS OF CASH FLOWS

(In Thousands)

(Unaudited)

	Six Months Ended April 30, 2015	2014
Cash flows from operating activities:		
Net loss	$(33,935)	$(32,425)
Adjustments to reconcile net loss to net cash used in operating activities:		
Depreciation	1,719	1,706
Compensation from stock options and awards	6,665	5,038
Amortization of bond discounts and deferred financing costs	5,991	4,913
Gain on sale and retirement of property and assets	(851)	(216)
Income from unconsolidated joint ventures	(2,918)	(3,638)
Distributions of earnings from unconsolidated joint ventures	4,445	491
Loss on extinguishment of debt	-	1,155
Inventory impairment and land option write-offs	6,541	1,186
Deferred income tax benefit	(15,975)	-
(Increase) decrease in assets:		
Mortgage loans held for sale at fair value	(11,114)	54,934
Restricted cash, receivables, prepaids, deposits and other assets	134	(4,354)
Inventories	(200,988)	(218,078)
(Decrease) increase in liabilities:		
State income tax payable	(70)	122
Customers' deposits	6,462	8,162
Accounts payable, accrued interest and other accrued liabilities	(22,235)	(5,102)
Net cash used in operating activities	(256,129)	(186,106)
Cash flows from investing activities:		
Proceeds from sale of property and assets	983	232
Purchase of property, equipment and other fixed assets and acquisitions	(1,172)	(1,048)
Decrease (increase) in restricted cash related to mortgage company	1,645	(376)
Investments in and advances to unconsolidated joint ventures	(15,539)	(32)
Distributions of capital from unconsolidated joint ventures	7,345	6,952
Net cash (used in) provided by investing activities	(6,738)	5,728
Cash flows from financing activities:		
Proceeds from mortgages and notes	76,569	64,301
Payments related to mortgages and notes	(61,858)	(35,401)
Proceeds from model sale leaseback financing programs	21,301	30,374
Payments related to model sale leaseback financing programs	(7,960)	(10,751)
Proceeds from land bank financing programs	4,144	8,666

Payments related to land bank financing programs	(17,147)	(22,484)
Proceeds from senior notes	250,000	150,000
Payments related to senior notes	-	(22,593)
Net proceeds (payments) related to mortgage warehouse lines of credit	6,047	(56,355)
Deferred financing costs from land bank financing programs and note issuances	(6,493)	(5,346)
Principal payments and debt repurchases	(2,062)	(4,005)
Net cash provided by financing activities	262,541	96,406
Net decrease in cash and cash equivalents	(326)	(83,972)
Cash and cash equivalents balance, beginning of period	261,898	329,204
Cash and cash equivalents balance, end of period	$261,572	$245,232

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HOVNANIAN ENTERPRISES, INC. AND SUBSIDIARIES

CONDENSED CONSOLIDATED STATEMENTS OF CASH FLOWS

(In Thousands - Unaudited)

(Continued)

	Six Months Ended April 30, 2015	2014
Supplemental disclosure of cash flow:		
Cash paid during the period for:		
Interest, net of capitalized interest (see Note 3 to the Condensed Consolidated Financial Statements)	$41,061	$43,939
Income taxes	$819	$1,104

See notes to condensed consolidated financial statements (unaudited).

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HOVNANIAN ENTERPRISES, INC. AND SUBSIDIARIES

NOTES TO CONDENSED CONSOLIDATED FINANCIAL STATEMENTS - UNAUDITED

1. Basis of Presentation

Hovnanian Enterprises, Inc. and Subsidiaries (the "Company", "we", "us" or "our") has reportable segments consisting of six Homebuilding segments (Northeast, Mid-Atlantic, Midwest, Southeast, Southwest and West) and the Financial Services segment (see Note 17).

The accompanying unaudited Condensed Consolidated Financial Statements include our accounts and those of all wholly-owned subsidiaries after elimination of all significant intercompany balances and transactions.

The accompanying unaudited Condensed Consolidated Financial Statements have been prepared in accordance with accounting principles generally accepted in the United States ("GAAP") for interim financial information and with the instructions to Form 10-Q and Article 10 of Regulation S-X and should be read in conjunction with the consolidated financial statements and notes thereto included in our Annual Report on Form 10-K for the fiscal year ended October 31, 2014. In the opinion of management, all adjustments for interim periods presented have been made, which include normal recurring accruals and deferrals necessary for a fair presentation of our condensed consolidated financial position, results of operations and cash flows. The preparation of Condensed Consolidated Financial Statements in conformity with GAAP requires management to make estimates and assumptions that affect the reported amounts of assets and liabilities and disclosure of contingent assets and liabilities at the date of the financial statements and the reported amounts of revenues and expenses during the reporting period. Actual results could differ from those estimates, and these differences could have a significant impact on the Condensed Consolidated Financial Statements. Results for interim periods are not necessarily indicative of the results which might be expected for a full year. The balance sheet at October 31, 2014 has been derived from the audited Consolidated Financial Statements at that date but does not include all of the information and footnotes required by GAAP for complete financial statements.

2. Stock Compensation

For the three and six months ended April 30, 2015, the Company's total stock-based compensation expense was $3.2 million and $6.7 million ($2.1 million and $4.6 million net of tax), respectively, and $1.5 million and $5.0 million for the three and six months ended April 30, 2014, respectively. Included in this total stock-based compensation expense was the vesting of stock options of $0.5 million and $1.4 million for the three and six months ended April 30, 2015, respectively, and $1.0 million and $2.0 million for the three and six months ended April 30, 2014, respectively.

3. Interest

Interest costs incurred, expensed and capitalized were:

	Three Months Ended		Six Months Ended	
	April 30,		April 30,	
(In thousands)	2015	2014	2015	2014
Interest capitalized at beginning of period	$114,241	$107,089	$109,158	$105,093
Plus interest incurred (1)	40,703	36,782	82,175	71,601
Less cost of sales interest expensed	12,013	12,407	23,331	21,897
Less other interest expensed (2)(3)	23,030	23,472	48,101	46,805
Interest capitalized at end of period (4)	$119,901	$107,992	$119,901	$107,992

(1) Data does not include interest incurred by our mortgage and finance subsidiaries.

(2) Other interest expensed includes interest that does not qualify for interest capitalization because our assets that qualify for interest capitalization (inventory under development) do not exceed our debt. Also includes interest on completed homes and land in planning, which does not qualify for capitalization, and therefore, is expensed.

(3) Cash paid for interest, net of capitalized interest, is the sum of other interest expensed, as defined above, and interest paid by our mortgage and finance subsidiaries adjusted for the change in accrued interest on notes payable, which is calculated as follows:

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(In thousands)	Three Months Ended April 30, 2015	2014	Six Months Ended April 30, 2015	2014
Other interest expensed	$23,030	$23,472	$48,101	$46,805
Interest paid by our mortgage and finance subsidiaries	268	409	676	1,145
Increase in accrued interest	(8,726)	(5,295)	(7,716)	(4,011)
Cash paid for interest, net of capitalized interest	$14,572	$18,586	$41,061	$43,939

(4) Capitalized interest amounts are shown gross before allocating any portion of impairments, if any, to capitalized interest.

4. Reduction of Inventory to Fair Value

We record impairment losses on inventories related to communities under development and held for future development when events and circumstances indicate that they may be impaired and the undiscounted cash flows estimated to be generated by those assets are less than their related carrying amounts. If the expected undiscounted cash flows are less than the carrying amount, then the community is written down to its fair value. We estimate the fair value of each impaired community by determining the present value of the estimated future cash flows at a discount rate commensurate with the risk of the respective community. For the six months ended April 30, 2015, our discount rate used for the impairments recorded ranged from 17.5% to 19.8%. For the six months ended April 30, 2014, no discount rate was used as the one community impaired during the quarter was land held for sale for which a purchase offer price was used to determine the fair value. This land was sold at the offer price in May 2014. Should the estimates or expectations used in determining cash flows or fair value decrease or differ from current estimates in the future, we may need to recognize additional impairments.

During the six months ended April 30, 2015, we evaluated inventories of all 508 communities under development and held for future development for impairment indicators through preparation and review of detailed budgets or other market indicators of impairment. We performed detailed impairment calculations for 15 of those communities (i.e., those with a projected operating loss or other impairment indicators) with an aggregate carrying value of $77.4 million. Of those communities tested for impairment, seven communities with an aggregate carrying value of $33.0 million had undiscounted future cash flows that exceeded the carrying amount by less than 20%. As a result of our impairment analysis, we recorded impairment losses of $3.5 million and $4.4 million, in four and five communities, respectively, with a pre-impairment value of $11.0 million and $16.7 million, respectively, for the three and six months ended April 30, 2015, respectively, and recorded $0.1 million, in one community with a pre-impairment value of $0.2 million, for both the three and six months ended April 30, 2014, which are included in the Condensed Consolidated Statements of Operations on the line entitled “Homebuilding: Inventory impairment loss and land option write-offs” and deducted from inventory. The pre-impairment value represents the carrying value, net of prior period impairments, if any, at the time of recording the impairment.

The Condensed Consolidated Statements of Operations line entitled “Homebuilding: Inventory impairment loss and land option write-offs” also includes write-offs of options and approval, engineering and capitalized interest costs that we record when we redesign communities and/or abandon certain engineering costs and we do not exercise options in various locations because the communities' pro forma profitability is not projected to produce adequate returns on investment commensurate with the risk. Total aggregate write-offs related to these items were $0.8 million and $0.4 million for the three months ended April 30, 2015 and 2014, respectively, and $2.1 million and $1.1 million for the six months ended April 30, 2015 and 2014, respectively. Occasionally, these write-offs are offset by recovered deposits (sometimes through legal action) that had been written off in a prior period as walk-away costs. Historically, these recoveries have not been significant in comparison to the total costs written off. The number of lots walked away from during the three months ended April 30, 2015 and 2014 were 455 and 894, respectively, and 2,155 and 2,430 during the six months ended April 30, 2015 and 2014, respectively.

We decide to mothball (or stop development on) certain communities when we determine that the current performance does not justify further investment at the time. When we decide to mothball a community, the inventory is reclassified on our Condensed Consolidated Balance Sheets from “Sold and unsold homes and lots under development” to “Land and land options held for future development or sale.” During the first half of fiscal 2015, we did not mothball any new communities, or re-activate or sell any communities which were previously mothballed. As of April 30, 2015, the net book value associated with our 45 total mothballed communities was $105.2 million, which was net of impairment charges recorded in prior periods of $412.4 million.

From time to time we enter into option agreements that include specific performance requirements, whereby we are required to purchase a minimum number of lots. Because of our obligation to purchase these lots, for accounting purposes in accordance with Accounting Standards Codification (“ASC”) 360-20-40-38, we are required to record this inventory on our Condensed Consolidated Balance Sheets. As of April 30, 2015, we had $1.7 million of specific performance options recorded on our Condensed Consolidated Balance Sheets to “Consolidated inventory not owned – specific performance options,” with a corresponding liability of $1.7 million recorded to “Liabilities from inventory not owned.”

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We sell and lease back certain of our model homes with the right to participate in the potential profit when each home is sold to a third party at the end of the respective lease. As a result of our continued involvement, for accounting purposes in accordance with ASC 360-20-40-38, these sale and leaseback transactions are considered a financing rather than a sale. Therefore, for purposes of our Condensed Consolidated Balance Sheets, at April 30, 2015, inventory of $83.2 million was recorded to “Consolidated inventory not owned – other options,” with a corresponding amount of $78.2 million recorded to “Liabilities from inventory not owned” for the amount of net cash received from the transactions.

We have land banking arrangements, whereby we sell our land parcels to the land banker and they provide us an option to purchase back finished lots on a quarterly basis. Because of our options to repurchase these parcels, for accounting purposes, in accordance with ASC 360-20-40-38, these transactions are considered a financing rather than a sale. For purposes of our Condensed Consolidated Balance Sheets, at April 30, 2015, inventory of $15.9 million was recorded as “Consolidated inventory not owned – other options,” with a corresponding amount of $11.1 million recorded to “Liabilities from inventory not owned” for the amount of net cash received from the transactions.

5. Variable Interest Entities

The Company enters into land and lot option purchase contracts to procure land or lots for the construction of homes. Under these contracts, the Company will fund a stated deposit in consideration for the right, but not the obligation, to purchase land or lots at a future point in time with predetermined terms. Under the terms of the option purchase contracts, many of the option deposits are not refundable at the Company's discretion. Under the requirements of ASC 810, certain option purchase contracts may result in the creation of a variable interest in the entity (“VIE”) that owns the land parcel under option.

In compliance with ASC 810, the Company analyzes its option purchase contracts to determine whether the corresponding land sellers are VIEs and, if so, whether the Company is the primary beneficiary. Although the Company does not have legal title to the underlying land, ASC 810 requires the Company to consolidate a VIE if the Company is determined to be the primary beneficiary. In determining whether it is the primary beneficiary, the Company considers, among other things, whether it has the power to direct the activities of the VIE that most significantly impact the VIE’s economic performance. Such activities would include, among other things, determining or limiting the scope or purpose of the VIE, selling or transferring property owned or controlled by the VIE, or arranging financing for the VIE. The Company also considers whether it has the obligation to absorb losses of the VIE or the right to receive benefits from the VIE. As a result of its analyses, the Company determined that as of April 30, 2015 and October 31, 2014, it was not the primary beneficiary of any VIEs from which it is purchasing land under option purchase contracts.

We will continue to secure land and lots using options, some of which are with VIEs. Including deposits on our unconsolidated VIEs, at April 30, 2015, we had total cash and letters of credit deposits amounting to $87.2 million to purchase land and lots with a total purchase price of $1.3 billion. The maximum exposure to loss with respect to our land and lot options is limited to the deposits plus any pre-development costs invested in the property, although some deposits are refundable at our request or refundable if certain conditions are not met.

6. Warranty Costs

General liability insurance for homebuilding companies and their suppliers and subcontractors is very difficult to obtain. The availability of general liability insurance is limited due to a decreased number of insurance companies willing to underwrite for the industry. In addition, those few insurers willing to underwrite liability insurance have significantly increased the premium costs. To date, we have been able to obtain general liability insurance but at higher premium costs with higher deductibles. Our subcontractors and suppliers have advised us that they have also had difficulty obtaining insurance that also provides us coverage. As a result, we have an owner controlled insurance program for certain of our subcontractors whereby the subcontractors pay us an insurance premium (through a reduction of amounts we would otherwise owe such subcontractors for their work on our homes) based on the risk type of the trade. We absorb the liability associated with their work on our homes as part of our overall general liability insurance at no additional cost to us because our existing general liability and construction defect insurance policy and related reserves for amounts under our deductible covers construction defects regardless of whether we or our subcontractors are responsible for the defect. For the six months ended April 30, 2015 and 2014, we received $1.3 million and $1.0 million, respectively, from subcontractors related to the owner controlled insurance program, which we accounted for as a reduction to inventory.

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We accrue for warranty costs that are covered under our existing general liability and construction defect policy as part of our general liability insurance deductible. This accrual is expensed as selling, general and administrative costs. For homes delivered in fiscal 2015 and 2014, our deductible under our general liability insurance is $20 million per occurrence for construction defect and warranty claims. For bodily injury claims, our deductible per occurrence in fiscal 2015 and 2014 is $0.25 million, up to a $5 million limit. Our aggregate retention in fiscal 2015 and 2014 is $21 million for construction defect, warranty and bodily injury claims. In addition, we establish a warranty accrual for lower cost related issues to cover home repairs, community amenities and land development infrastructure that are not covered under our general liability and construction defect policy. We accrue an estimate for these warranty costs as part of cost of sales at the time each home is closed and title and possession have been transferred to the homebuyer. Additions and charges in the warranty reserve and general liability reserve for the three and six months ended April 30, 2015 and 2014 were as follows:

	Three Months Ended April 30,		Six Months Ended April 30,	
(In thousands)	2015	2014	2015	2014
Balance, beginning of period	$181,833	$133,077	$178,008	$131,028
Additions – Selling, general and administrative	4,331	4,510	9,580	9,051
Additions – Cost of sales	5,635	2,082	8,816	4,128
Charges incurred during the period	(30,492)	(4,804)	(35,097)	(9,342)
Changes to pre-existing reserves	-	-	-	-
Balance, end of period	$161,307	$134,865	$161,307	$134,865

Warranty accruals are based upon historical experience. We engage a third-party actuary that uses our historical warranty and construction defect data, worker's compensation data and other industry data to assist us in estimating our reserves for unpaid claims, claim adjustment expenses and incurred but not reported claims reserves for the risks that we are assuming under the general liability and workers compensation programs. The estimates include provisions for inflation, claims handling, and legal fees.

Insurance claims paid by our insurance carriers, excluding insurance deductibles paid, were $18.1 million and $1.3 million for the three months ended April 30, 2015 and 2014, respectively, and $18.3 million and $4.2 million for the six months ended April 30, 2015 and 2014, respectively, for prior year deliveries. During the three months ended April 30, 2015 we settled the D'Andrea class action suit with the majority of the settlement being paid by our insurance carriers. See Note 7 below.

7. Commitments and Contingent Liabilities

We are involved in litigation arising in the ordinary course of business, none of which is expected to have a material effect on our financial position, results of operations or cash flows, and we are subject to extensive and complex regulations that affect the development and home building, sales and customer financing processes, including zoning, density, building standards and mortgage financing. These regulations often provide broad discretion to the administering governmental authorities. This can delay or increase the cost of development or homebuilding.

We also are subject to a variety of local, state, federal and foreign laws and regulations concerning protection of health and the environment, including those regulating the emission or discharge of materials into the environment, the management of stormwater runoff at construction sites, the handling, use, storage and disposal of hazardous substances, impacts to wetlands and other sensitive environments, and the remediation of contamination at properties that we have owned or developed or currently own or are developing (“environmental laws”). The particular environmental laws that apply to any given community vary greatly according to the community site, the site’s environmental conditions and the present and former uses of the site. These environmental laws may result in delays, may cause us to incur substantial compliance, remediation and/or other costs, and can prohibit or severely restrict development and homebuilding activity. In addition, noncompliance with these laws and regulations could result in fines and penalties, obligations to remediate, permit revocations or other sanctions; and contamination or other environmental conditions at or in the vicinity of our developments may result in claims against us for personal injury, property damage or other losses.

In March 2013, we received a letter from the Environmental Protection Agency (“EPA”) requesting information about our involvement in a housing redevelopment project in Newark, New Jersey that a Company entity undertook during the 1990s. We understand that the development is in the vicinity of a former lead smelter and that recent tests on soil samples from properties within the development conducted by the EPA show elevated levels of lead. We also understand that the smelter ceased operations many years before the Company entity involved acquired the properties in the area and carried out the re-development project. We responded to the EPA’s request. In August 2013, we were notified that the EPA considers us a potentially responsible party (or “PRP”) with respect to the site, that the EPA will clean up the site, and that the EPA is proposing that we fund and/or contribute towards the cleanup of the contamination at the site. We have begun preliminary discussions with the EPA concerning a possible resolution but do not know the scope or extent of the Company’s obligations, if any, that may arise from the site and therefore cannot provide any assurance that this matter will not have a material impact on the Company. The EPA requested additional information in April 2014 and the Company has responded to its information request.

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We anticipate that increasingly stringent requirements will be imposed on developers and homebuilders in the future. Although we cannot reliably predict the extent of any effect these requirements may have on us, they could result in time-consuming and expensive compliance programs and in substantial expenditures, which could cause delays and increase our cost of operations. In addition, our ability to obtain or renew permits or approvals and the continued effectiveness of permits already granted or approvals already obtained is dependent upon many factors, some of which are beyond our control, such as changes in policies, rules and regulations and their interpretations and application.

The Company was also involved in the following litigation: Hovnanian Enterprises, Inc. and K. Hovnanian Venture I, L.L.C. (collectively, the “Company Defendants”) were named as defendants in a class action suit. The action was filed by Mike D’Andrea and Tracy D’Andrea, on behalf of themselves and all others similarly situated in the Superior Court of New Jersey, Gloucester County. The action was initially filed on May 8, 2006 alleging that the HVAC systems installed in certain of the Company’s homes are in violation of applicable New Jersey building codes and are a potential safety issue. On December 14, 2011, the Superior Court granted class certification; the potential class is 1,065 homes. The Company Defendants filed a request to take an interlocutory appeal regarding the class certification decision. The Appellate Division denied the request, and the Company Defendants filed a request for interlocutory review by the New Jersey Supreme Court, which remanded the case back to the Appellate Division for a review on the merits of the appeal on May 8, 2012. The Appellate Division, on remand, heard oral arguments on December 4, 2012, reviewing the Superior Court’s original finding of class certification. On June 18, 2013, the Appellate Division affirmed class certification. On July 3, 2013, the Company Defendants appealed the June 2013 Appellate Division’s decision to the New Jersey Supreme Court, which elected not to hear the appeal on October 22, 2013. The plaintiff class was seeking unspecified damages as well as treble damages pursuant to the NJ Consumer Fraud Act. The Company Defendants’ motion to consolidate an indemnity action they filed against various manufacturer and sub-contractor defendants to require these parties to participate directly in the class action was denied by the Superior Court; however, the Company Defendants’ separate action seeking indemnification against the various manufacturers and subcontractors implicated by the class action is ongoing. The Company Defendants, the Company Defendants’ insurance carriers and the plaintiff class agreed to the terms of a settlement on May 15, 2014 in which the plaintiff class was to receive a payment of $21 million in settlement of all claims, with the majority of the settlement being funded by the Company Defendants’ insurance carriers. The Company had previously reserved for its share of the settlement. The Superior Court approved the settlement agreement on December 23, 2014, and the judgment became final on February 20, 2015, when no appeal was taken. The settlement amount was paid in full and the class action matter is now concluded.

8. Restricted Cash and Deposits

Cash represents cash deposited in checking accounts. Cash equivalents include certificates of deposit, Treasury bills and government money–market funds with maturities of 90 days or less when purchased. Our cash balances are held at a few financial institutions and may, at times, exceed insurable amounts. We believe we help to mitigate this risk by depositing our cash in major financial institutions. At April 30, 2015 and October 31, 2014, $12.7 million and $15.4 million, respectively, of the total cash and cash equivalents was in cash equivalents, the book value of which approximated fair value.

Restricted cash and cash equivalents on the Condensed Consolidated Balance Sheets totaled $23.6 million and $29.3 million as of April 30, 2015 and October 31, 2014, respectively, which included cash collateralizing our letter of credit agreements and facilities and is discussed in Note 10. Also included in this balance were homebuilding and financial services customers' deposits of $7.0 million and $14.0 million at April 30, 2015, respectively, and $7.5 million and $15.8 million as of October 31, 2014, respectively, which are restricted from use by us.

Total Homebuilding Customers' deposits are shown as a liability on the Condensed Consolidated Balance Sheets. These liabilities are significantly more than the applicable periods' restricted cash balances because in some states, the deposits are not restricted from use and, in other states, we are able to release the majority of these customer deposits to cash by pledging letters of credit and surety bonds.

9. Mortgage Loans Held for Sale

Our mortgage banking subsidiary originates mortgage loans, primarily from the sale of our homes. Such mortgage loans are sold in the secondary mortgage market within a short period of time of origination. Mortgage loans held for sale consist primarily of single-family residential loans collateralized by the underlying property. We have elected the fair value option to record loans held for sale and therefore these loans are recorded at fair value with the changes in the value recognized in the Condensed Consolidated Statements of Operations in "Revenues: Financial services." We currently use forward sales of mortgage-backed securities ("MBS"), interest rate commitments from borrowers and mandatory and/or best efforts forward commitments to sell loans to third-party purchasers to protect us from interest rate fluctuations. These short-term instruments, which do not require any payments to be made to the counterparty or purchaser in connection with the execution of the commitments, are recorded at fair value. Gains and losses on changes in the fair value are recognized in the Condensed Consolidated Statements of Operations in "Revenues: Financial services."

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At April 30, 2015 and October 31, 2014, $86.5 million and $78.6 million, respectively, of mortgages held for sale were pledged against our mortgage warehouse lines of credit (see Note 10). We may incur losses with respect to mortgages that were previously sold that are delinquent and which had underwriting defects, but only to the extent the losses are not covered by mortgage insurance or the resale value of the home. The reserves for these estimated losses are included in the "Financial services – Accounts payable and other liabilities" balances on the Condensed Consolidated Balance Sheets. As of April 30, 2015 and 2014, we had reserves specifically for 131 and 217 identified mortgage loans, respectively, as well as reserves for an estimate for future losses on mortgages sold but not yet identified to us.

The activity in our loan origination reserves during the three and six months ended April 30, 2015 and 2014 was as follows:

(In thousands)	Three Months Ended April 30, 2015	2014	Six Months Ended April 30, 2015	2014
Loan origination reserves, beginning of period	$7,981	$10,719	$7,352	$11,036
Provisions for losses during the period	68	466	129	867
Adjustments to pre-existing provisions for losses from changes in estimates	(107)	(63)	461	(622)
Payments/settlements	-	(65)	-	(224)
Loan origination reserves, end of period	$7,942	$11,057	$7,942	$11,057

10. Mortgage and Notes Payable

We have nonrecourse mortgage loans for certain communities totaling $118.9 million and $103.9 million at April 30, 2015 and October 31, 2014, respectively, which are secured by the related real property, including any improvements, with an aggregate book value of approximately $321.2 million and $220.1 million, respectively. The weighted-average interest rate on these obligations was 5.0% at both April 30, 2015 and October 31, 2014, and the mortgage loan payments on each community primarily correspond to home deliveries. We also have nonrecourse mortgage loans on our corporate headquarters totaling $16.1 million and $16.6 million at April 30, 2015 and October 31, 2014, respectively. These loans had a weighted-average interest rate of 8.7% and 7.0% at April 30, 2015 and October 31, 2014, respectively. As of April 30, 2015, these loans had installment obligations with annual principal maturities in the years ending October 31 of approximately: $0.6 million in 2015, $1.2 million in 2016, $1.3 million in 2017, $1.4 million in 2018, $1.5 million in 2019 and $10.1 million after 2019.

In June 2013, K. Hovnanian Enterprises, Inc. ("K. Hovnanian"), as borrower, and we and certain of our subsidiaries, as guarantors, entered into a five-year, $75.0 million unsecured revolving credit facility (the "Credit Facility") with Citicorp USA, Inc., as administrative agent and issuing bank, and Citibank, N.A., as a lender. The Credit Facility is available for both letters of credit and general corporate purposes. The Credit Facility does not contain any financial maintenance covenants, but does contain certain restrictive covenants that track those contained in our indenture governing the 8.0% Senior Notes due 2019, which are described in Note 11. The Credit Facility also contains certain customary events of default which would permit the administrative agent at the request of the required lenders to, among other things, declare all loans then outstanding to be immediately due and payable if such default is not cured within applicable grace periods, including the failure to make timely payments of amounts payable under the Credit Facility or other material indebtedness or the acceleration of other material indebtedness, the failure to comply with agreements and covenants or for representations or warranties to be correct in all material respects when made, specified events of bankruptcy and insolvency, and the entry of a material judgment against a loan party. Outstanding borrowings under the Credit Facility accrue interest at an annual rate equal to either, as selected by K. Hovnanian, (i) the alternate base rate plus the applicable spread determined on the date of such borrowing or (ii) an adjusted London Interbank Offered Rate (“LIBOR”) rate plus the applicable spread determined as of the date two business days prior to the first day of the interest period for such borrowing. As of April 30, 2015 and October 31, 2014, there were no borrowings and $22.4 million and $26.5 million, respectively, of letters of credit outstanding under the Credit Facility. As of April 30, 2015, we believe we were in compliance with the covenants under the Credit Facility.

In addition to the Credit Facility, we have certain stand–alone cash collateralized letter of credit agreements and facilities under which there were a total of $2.6 million and $5.5 million letters of credit outstanding at April 30, 2015 and October 31, 2014, respectively. These agreements and facilities require us to maintain specified amounts of cash as collateral in segregated accounts to support the letters of credit issued thereunder, which will affect the amount of cash we have available for other uses. As of April 30, 2015 and October 31, 2014, the amount of cash collateral in these segregated accounts was $2.6 million and $5.6 million, respectively, which is reflected in “Restricted cash and cash equivalents” on the Condensed Consolidated Balance Sheets.

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Our wholly owned mortgage banking subsidiary, K. Hovnanian American Mortgage, LLC ("K. Hovnanian Mortgage"), originates mortgage loans primarily from the sale of our homes. Such mortgage loans and related servicing rights are sold in the secondary mortgage market within a short period of time. In certain instances, we retain the servicing rights for a small amount of loans. Our secured Master Repurchase Agreement with JPMorgan Chase Bank, N.A. ("Chase Master Repurchase Agreement"), which was amended on January 30, 2015, is a short-term borrowing facility that provides up to $50.0 million through January 30, 2016. The loan is secured by the mortgages held for sale and is repaid when we sell the underlying mortgage loans to permanent investors. Interest is payable monthly on outstanding advances at an adjusted LIBOR rate, which was 0.18% at April 30, 2015, plus the applicable margin of 2.75%. Therefore, at April 30, 2015, the interest rate was 2.93%. As of April 30, 2015 and October 31, 2014, the aggregate principal amount of all borrowings outstanding under the Chase Master Repurchase Agreement was $31.9 million and $25.5 million, respectively.

K. Hovnanian Mortgage has another secured Master Repurchase Agreement with Customers Bank ("Customers Master Repurchase Agreement"), which was amended on February 19, 2015 to extend the maturity date to February 18, 2016, that is a short-term borrowing facility that provides up to $37.5 million through maturity. The loan is secured by the mortgages held for sale and is repaid when we sell the underlying mortgage loans to permanent investors. Interest is payable daily or as loans are sold to permanent investors on outstanding advances at the current LIBOR, plus the applicable margin ranging from 2.75% to 5.25% based on the takeout investor, type of loan, and the number of days on the warehouse line. As of April 30, 2015 and October 31, 2014, the aggregate principal amount of all borrowings outstanding under the Customers Master Repurchase Agreement was $27.2 million and $20.4 million, respectively.

K. Hovnanian Mortgage has a third secured Master Repurchase Agreement with Credit Suisse First Boston Mortgage Capital LLC ("Credit Suisse Master Repurchase Agreement"), which was last amended on November 17, 2014, that is a short-term borrowing facility that provides up to $50.0 million through October 27, 2015. The facility also provides an additional $30.0 million which can be used between 10 calendar days prior to the end of a fiscal quarter through the 45th calendar day after a fiscal quarter end; provided that the amount outstanding may not exceed $50.0 million outside of this date range. The loan is secured by the mortgages held for sale and is repaid when we sell the underlying mortgage loans to permanent investors. Interest is payable monthly on outstanding advances at the Credit Suisse Cost of Funds, which was 0.47% at April 30, 2015, plus the applicable margin ranging from 2.25% to 2.75% based on the takeout investor, type of loan and the number of days outstanding. As of April 30, 2015 and October 31, 2014, the aggregate principal amount of all borrowings outstanding under the Credit Suisse Master Repurchase Agreement was $11.0 million and $19.7 million, respectively.

In February 2014, K. Hovnanian Mortgage executed a secured Master Repurchase Agreement with Comerica Bank ("Comerica Master Repurchase Agreement"), which was amended on December 30, 2014 to extend the maturity date to December 29, 2015, that is a short-term borrowing facility that provides up to $35.0 million through maturity. The loan is secured by the mortgages held for sale and is repaid when we sell the underlying mortgage loans to permanent investors. Interest is payable monthly at LIBOR, subject to a floor of 0.25%, plus the applicable margin of 2.625%. As of April 30, 2015 and October 31, 2014, the interest rate was 2.875% and the aggregate principal amount of all borrowings outstanding under the Comerica Master Repurchase Agreement was $12.8 million and $11.3 million, respectively.

The Chase Master Repurchase Agreement, Customers Master Repurchase Agreement, Credit Suisse Master Repurchase Agreement and Comerica Master Repurchase Agreement (together, the “Master Repurchase Agreements”) require K. Hovnanian Mortgage to satisfy and maintain specified financial ratios and other financial condition tests. Because of the extremely short period of time mortgages are held by K. Hovnanian Mortgage before the mortgages are sold to investors (generally a period of a few weeks), the immateriality to us on a consolidated basis of the size of the Master Repurchase Agreements, the levels required by these financial covenants, our ability based on our immediately available resources to contribute sufficient capital to cure any default, were such conditions to occur, and our right to cure any conditions of default based on the terms of the agreement, we do not consider any of these covenants to be substantive or material. As of April 30, 2015, we believe we were in compliance with the covenants under the Master Repurchase Agreements.

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11. Senior Secured, Senior, Senior Amortizing and Senior Exchangeable Notes

Senior Secured, Senior, Senior Amortizing and Senior Exchangeable Notes balances as of April 30, 2015 and October 31, 2014, were as follows:

(In thousands)	**April 30, 2015**	**October 31, 2014**
Senior Secured Notes:		
7.25% Senior Secured First Lien Notes due October 15, 2020	$577,000	$577,000
9.125% Senior Secured Second Lien Notes due November 15, 2020	220,000	220,000
2.0% Senior Secured Notes due November 1, 2021 (net of discount)	53,133	53,129
5.0% Senior Secured Notes due November 1, 2021 (net of discount)	130,496	129,806
Total Senior Secured Notes	$980,629	$979,935
Senior Notes:		
11.875% Senior Notes due October 15, 2015 (net of discount)	60,620	60,414
6.25% Senior Notes due January 15, 2016 (net of discount)	172,656	172,483
7.5% Senior Notes due May 15, 2016	86,532	86,532
8.625% Senior Notes due January 15, 2017	121,043	121,043
7.0% Senior Notes due January 15, 2019	150,000	150,000
8.0% Senior Notes due November 1, 2019	250,000	-
Total Senior Notes	$840,851	$590,472
11.0% Senior Amortizing Notes due December 1, 2017	$14,987	$17,049
Senior Exchangeable Notes due December 1, 2017	$71,913	$70,101

Except for K. Hovnanian, the issuer of the notes, our home mortgage subsidiaries, joint ventures and subsidiaries holding interests in our joint ventures, certain of our title insurance subsidiaries and our foreign subsidiary, we and each of our subsidiaries are guarantors of the senior secured, senior, senior amortizing and senior exchangeable notes outstanding at April 30, 2015 (see Note 21). In addition, the 5.0% Senior Secured Notes due 2021 (the "5.0% 2021 Notes") and the 2.0% Senior Secured Notes due 2021 (the "2.0% 2021 Notes" and together with the 5.0% 2021 Notes, the "2021 Notes") are guaranteed by K. Hovnanian JV Holdings, L.L.C. and its subsidiaries except for certain joint ventures and joint venture holding companies (collectively, the "Secured Group"). Members of the Secured Group do not guarantee K. Hovnanian's other indebtedness.

The indentures governing the notes do not contain any financial maintenance covenants, but do contain restrictive covenants that limit, among other things, the Company's ability and that of certain of its subsidiaries, including K. Hovnanian, to incur additional indebtedness (other than certain permitted indebtedness, refinancing indebtedness and nonrecourse indebtedness), pay dividends and make distributions on common and preferred stock, repurchase subordinated indebtedness (with respect to certain of the senior secured and senior notes), make other restricted payments, make investments, sell certain assets, incur liens, consolidate, merge, sell or otherwise dispose of all or substantially all assets, and enter into certain transactions with affiliates. The indentures also contain events of default which would permit the holders of the notes to declare the notes to be immediately due and payable if not cured within applicable grace periods, including the failure to make timely payments on the notes or other material indebtedness, the failure to comply with agreements and covenants and specified events of bankruptcy and insolvency and, with respect to the indentures governing the senior secured notes, the failure of the documents granting security for the senior secured notes to be in full force and effect, and the failure of the liens on any material portion of the collateral securing the senior secured notes to be valid and perfected. As of April 30, 2015, we believe we were in compliance with the covenants of the indentures governing our outstanding notes.

Under the terms of the indentures, we have the right to make certain redemptions and, depending on market conditions and covenant restrictions, may do so from time to time. We also continue to evaluate our capital structure and may also continue to make debt purchases and/or exchanges for debt or equity from time to time through tender offers, open market purchases, private transactions, or otherwise, or seek to raise additional debt or equity capital, depending on market conditions and covenant restrictions.

If our consolidated fixed charge coverage ratio, as defined in the indentures governing our senior secured and senior notes (other than the senior exchangeable notes discussed in Note 12 below), is less than 2.0 to 1.0, we are restricted from making certain payments, including dividends, and from incurring indebtedness other than certain permitted indebtedness, refinancing indebtedness, and nonrecourse indebtedness. As a result of this restriction, we are currently restricted from paying dividends, which are not cumulative, on our 7.625% Series A Preferred Stock. We anticipate that we will continue to be restricted from paying dividends for the foreseeable future. Our inability to pay dividends is in accordance with covenant restrictions and will not result in a default under our debt instruments or otherwise affect compliance with any of the covenants contained in our debt instruments.

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The 7.25% Senior Secured First Lien Notes due 2020 (the “First Lien Notes”) are secured by a first-priority lien and the 9.125% Senior Secured Second Lien Notes due 2020 (the “Second Lien Notes” and, together with the First Lien Notes, the “2020 Secured Notes”) are secured by a second-priority lien, in each case, subject to permitted liens and other exceptions, on substantially all the assets owned by us, K. Hovnanian and the guarantors of such notes. At April 30, 2015, the aggregate book value of the real property that constituted collateral securing the 2020 Secured Notes was approximately $786.2 million, which does not include the impact of inventory investments, home deliveries, or impairments thereafter and which may differ from the value if it were appraised. In addition, cash and cash equivalents collateral that secured the 2020 Secured Notes was $221.1 million as of April 30, 2015, which included $2.6 million of restricted cash collateralizing certain letters of credit. Subsequent to such date, cash uses include general business operations and real estate and other investments.

The guarantees with respect to the 2021 Notes of the Secured Group are secured, subject to permitted liens and other exceptions, by a first-priority lien on substantially all of the assets of the members of the Secured Group. As of April 30, 2015, the collateral securing the guarantees included (1) $38.3 million of cash and cash equivalents (subsequent to such date, cash uses include general business operations and real estate and other investments); (2) approximately $141.0 million aggregate book value of real property of the Secured Group, which does not include the impact of inventory investments, home deliveries or impairments thereafter and which may differ from the value if it were appraised, and (3) equity interests in guarantors that are members of the Secured Group. Members of the Secured Group also own equity in joint ventures, either directly or indirectly through ownership of joint venture holding companies, with a book value of $66.7 million as of April 30, 2015; this equity is not pledged to secure, and is not collateral for, the 2021 Notes. Members of the Secured Group are “unrestricted subsidiaries” under K. Hovnanian's other senior notes and senior secured notes, and thus have not guaranteed such indebtedness.

On January 10, 2014, K. Hovnanian issued $150.0 million aggregate principle amount of 7.0% Senior Notes due 2019, resulting in net proceeds of approximately $147.8 million. The notes are redeemable in whole or in part at our option at any time prior to July 15, 2016 at 100% of their principal amount plus an applicable “Make-Whole Amount.” We may also redeem some or all of the notes at 103.5% of principal commencing July 15, 2016, at 101.75% of principal commencing January 15, 2017 and 100% of principal commencing January 15, 2018. In addition, we may redeem up to 35% of the aggregate principal amount of the notes prior to July 15, 2016 with the net cash proceeds from certain equity offerings at 107.0% of principal. We used a portion of the net proceeds to fund the redemption on February 9, 2014 (effected on February 10, 2014 which was the next business day after the redemption date) of the remaining outstanding principal amount ($21.4 million) of our 6.25% Senior Notes due 2015. The redemption resulted in a loss on extinguishment of debt of $1.2 million, net of the write-off of unamortized fees, and was included in the Condensed Consolidated Statement of Operations as “Loss on extinguishment of debt” in the second quarter of fiscal 2014. The remaining net proceeds from the offering were used to pay related fees and expenses and for general corporate purposes.

On November 5, 2014, K. Hovnanian issued $250.0 million aggregate principal amount of 8.0% Senior Notes due 2019, resulting in net proceeds of $245.7 million. These proceeds were used for general corporate purposes. The notes will mature on November 1, 2019. The notes are redeemable in whole or in part at K. Hovnanian’s option at any time prior to August 1, 2019 at a redemption price equal to 100% of their principal amount plus an applicable “Make-Whole

Amount." At any time and from time to time on or after August 1, 2019, K. Hovnanian may also redeem some or all of the notes to a redemption price equal to 100% of their principal amount.

12. Senior Exchangeable Notes

On October 2, 2012, the Company and K. Hovnanian issued $100,000,000 aggregate stated amount of 6.0% Exchangeable Note Units (the "Units") (equivalent to 100,000 Units). Each $1,000 stated amount of Units initially consists of (1) a zero coupon senior exchangeable note due December 1, 2017 (a "Senior Exchangeable Note") issued by K. Hovnanian, which bears no cash interest and has an initial principal amount of $768.51 per Senior Exchangeable Note, and that will accrete to $1,000 at maturity and (2) a senior amortizing note due December 1, 2017 (a "Senior Amortizing Note") issued by K. Hovnanian, which has an initial principal amount of $231.49 per Senior Amortizing Note, bears interest at a rate of 11.0% per annum, and has a final installment payment date of December 1, 2017. Each Unit may be separated into its constituent Senior Exchangeable Note and Senior Amortizing Note after the initial issuance date of the Units, and the separate components may be combined to create a Unit.

Each Senior Exchangeable Note had an initial principal amount of $768.51 (which will accrete to $1,000 over the term of the Senior Exchangeable Note at an annual rate of 5.17% from the date of issuance, calculated on a semi-annual bond equivalent yield basis). Holders may exchange their Senior Exchangeable Notes at their option at any time prior to 5:00 p.m., New York City time, on the business day immediately preceding December 1, 2017. Each Senior Exchangeable Note will be exchangeable for shares of Class A Common Stock at an initial exchange rate of 185.5288 shares of Class A Common Stock per Senior Exchangeable Note (equivalent to an initial exchange price, based on $1,000 principal amount at maturity, of approximately $5.39 per share of Class A Common Stock). The exchange rate will be subject to adjustment in certain events. If certain corporate events occur prior to the maturity date, the Company will increase the applicable exchange rate for any holder who elects to exchange its Senior Exchangeable Notes in connection with such corporate event. In addition, holders of Senior Exchangeable Notes will also have the right to require K. Hovnanian to repurchase such holders' Senior Exchangeable Notes upon the occurrence of certain of these corporate events. As of April 30, 2015, 18,305 Senior Exchangeable Notes have been converted into 3.4 million shares of our Class A Common Stock, all of which were converted during the first quarter of fiscal 2013.

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On each June 1 and December 1 (each, an "installment payment date"), K. Hovnanian will pay holders of Senior Amortizing Notes equal semi-annual cash installments of $30.00 per Senior Amortizing Note (except for the June 1, 2013 installment payment, which was $39.83 per Senior Amortizing Note), which cash payment in the aggregate will be equivalent to 6.0% per year with respect to each $1,000 stated amount of Units. Each installment will constitute a payment of interest (at a rate of 11.0% per annum) and a partial repayment of principal on the Senior Amortizing Note. Following certain corporate events that occur prior to the maturity date, holders of the Senior Amortizing Notes will have the right to require K. Hovnanian to repurchase such holders' Senior Amortizing Notes.

13. Per Share Calculation

Basic earnings per share is computed by dividing net income (loss) (the "numerator") by the weighted-average number of common shares outstanding, adjusted for nonvested shares of restricted stock (the "denominator") for the period. The basic weighted–average number of shares for the three and six months ended April 30, 2014 included 6.1 million shares related to Purchase Contracts (issued as part of our then outstanding 7.25% Tangible Equity Units) which shares were issued upon settlement of the Purchase Contracts in February 2014. Computing diluted earnings per share is similar to computing basic earnings per share, except that the denominator is increased to include the dilutive effects of options and nonvested shares of restricted stock, as well as common shares issuable upon exchange of our Senior Exchangeable Notes issued as part of our 6.0% Exchangeable Note Units. Any options that have an exercise price greater than the average market price are considered to be anti-dilutive and are excluded from the diluted earnings per share calculation.

All outstanding nonvested shares that contain nonforfeitable rights to dividends or dividend equivalents that participate in undistributed earnings with common stock are considered participating securities and are included in computing earnings per share pursuant to the two-class method. The two-class method is an earnings allocation formula that determines earnings per share for each class of common stock and participating securities according to dividends or dividend equivalents and participation rights in undistributed earnings in periods when we have net income. The Company's restricted common stock ("nonvested shares") are considered participating securities.

Incremental shares attributed to nonvested stock and outstanding options to purchase common stock of 0.3 million for the six months ended April 30, 2015, and 0.9 million and 1.0 million for the three and six months ended April 30, 2014, respectively, were excluded from the computation of diluted earnings per share because we had a net loss for the period, and any incremental shares would not be dilutive. There were no incremental shares attributed to nonvested stock and outstanding options to purchase common stock for the three months ended April 30, 2015. Also, for both the three and six months ended April 30, 2015 and 2014, 15.2 million shares of common stock issuable upon the exchange of our Senior Exchangeable Notes (which were issued in fiscal 2012) were excluded from the computation of diluted earnings per share because we had net losses for the periods.

In addition, shares related to out-of-the money stock options that could potentially dilute basic earnings per share in the future that were not included in the computation of diluted earnings per share were 3.3 million for the three and six months ended April 30, 2015, and 2.2 million for the three and six months ended April 30, 2014, because to do so would have been anti-dilutive for the periods presented.

14. Preferred Stock

On July 12, 2005, we issued 5,600 shares of 7.625% Series A Preferred Stock, with a liquidation preference of $25,000 per share. Dividends on the Series A Preferred Stock are not cumulative and are paid at an annual rate of 7.625%. The Series A Preferred Stock is not convertible into the Company’s common stock and is redeemable in whole or in part at our option at the liquidation preference of the shares. The Series A Preferred Stock is traded as depositary shares, with each depositary share representing 1/1000th of a share of Series A Preferred Stock. The depositary shares are listed on the NASDAQ Global Market under the symbol “HOVNP.” During the three and six months ended April 30, 2015 and 2014, we did not pay any dividends on the Series A Preferred Stock due to covenant restrictions in our debt instruments.

15. Common Stock

Each share of Class A Common Stock entitles its holder to one vote per share, and each share of Class B Common Stock generally entitles its holder to ten votes per share. The amount of any regular cash dividend payable on a share of Class A Common Stock will be an amount equal to 110% of the corresponding regular cash dividend payable on a share of Class B Common Stock. If a shareholder desires to sell shares of Class B Common Stock, such stock must be converted into shares of Class A Common Stock.

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On August 4, 2008, our Board of Directors adopted a shareholder rights plan (the “Rights Plan”) designed to preserve shareholder value and the value of certain tax assets primarily associated with net operating loss (NOL) carryforwards and built-in losses under Section 382 of the Internal Revenue Code. Our ability to use NOLs and built-in losses would be limited if there was an “ownership change” under Section 382. This would occur if shareholders owning (or deemed under Section 382 to own) 5% or more of our stock increase their collective ownership of the aggregate amount of our outstanding shares by more than 50 percentage points over a defined period of time. The Rights Plan was adopted to reduce the likelihood of an “ownership change” occurring as defined by Section 382. Under the Rights Plan, one right was distributed for each share of Class A Common Stock and Class B Common Stock outstanding as of the close of business on August 15, 2008. Effective August 15, 2008, if any person or group acquires 4.9% or more of the outstanding shares of Class A Common Stock without the approval of the Board of Directors, there would be a triggering event causing significant dilution in the voting power of such person or group. However, existing stockholders who owned, at the time of the Rights Plan’s adoption, 4.9% or more of the outstanding shares of Class A Common Stock will trigger a dilutive event only if they acquire additional shares. The approval of the Board of Directors’ decision to adopt the Rights Plan may be terminated by the Board of Directors at any time, prior to the Rights being triggered. The Rights Plan will continue in effect until August 15, 2018, unless it expires earlier in accordance with its terms. The approval of the Board of Directors’ decision to adopt the Rights Plan was submitted to a stockholder vote and approved at a special meeting of stockholders held on December 5, 2008. Also at the Special Meeting on December 5, 2008, our stockholders approved an amendment to our Certificate of Incorporation to restrict certain transfers of Class A Common Stock in order to preserve the tax treatment of our NOLs and built-in losses under Section 382 of the Internal Revenue Code. Subject to certain exceptions pertaining to pre-existing 5% stockholders and Class B stockholders, the transfer restrictions in the amended Certificate of Incorporation generally restrict any direct or indirect transfer (such as transfers of our stock that result from the transfer of interests in other entities that own our stock) if the effect would be to (i) increase the direct or indirect ownership of our stock by any person (or public group) from less than 5% to 5% or more of our common stock; (ii) increase the percentage of our common stock owned directly or indirectly by a person (or public group) owning or deemed to own 5% or more of our common stock; or (iii) create a new public group. Transfers included under the transfer restrictions include sales to persons (or public groups) whose resulting percentage ownership (direct or indirect) of common stock would exceed the 5% thresholds discussed above, or to persons whose direct or indirect ownership of common stock would by attribution cause another person (or public group) to exceed such threshold.

On July 3, 2001, our Board of Directors authorized a stock repurchase program to purchase up to 4 million shares of Class A Common Stock. There were no shares purchased during the three and six months ended April 30, 2015. As of April 30, 2015, the maximum number of shares of Class A Common Stock that may yet be purchased under this program is 0.5 million.

16. Income Taxes

The total income tax benefit of $9.9 million and $15.2 million recognized for the three and six months ended April 30, 2015, respectively, was primarily due to deferred taxes partially offset by state tax expenses and state tax reserves for uncertain tax positions. The total income tax expense of $0.6 million and $1.2 million recognized for the three and six months ended April 30, 2014, respectively, was primarily due to various state tax expenses and state tax reserves for uncertain tax positions.

Deferred federal and state income tax assets primarily represent the deferred tax benefits arising from temporary differences between book and tax income which will be recognized in future years as an offset against future taxable income. If the combination of future years' income (or loss) and the reversal of the timing differences results in a loss, such losses can be carried forward to future years. In accordance with ASC 740, we evaluate our deferred tax assets quarterly to determine if valuation allowances are required. ASC 740 requires that companies assess whether valuation allowances should be established based on the consideration of all available evidence using a "more likely than not" standard.

As of October 31, 2014, and again at April 30, 2015, we concluded that it was more likely than not that a substantial amount of our deferred tax assets ("DTA") would be utilized. This conclusion was based on a detailed evaluation of all relevant evidence, both positive and negative. The positive evidence included factors such as positive earnings for the last two full fiscal years and the expectation of earnings going forward over the long term and evidence of a sustained recovery in the housing markets in which we operate. Such evidence is supported by significant increases in key financial indicators over the last few years, including new orders, revenues, backlog, community count and deliveries compared with the prior years. Economic data has also been affirming the housing market recovery. Housing starts, homebuilding volume and prices are increasing and forecasted to continue to increase. Historically low mortgage rates, affordable home prices, reduced foreclosures and a favorable home ownership to rental comparison are key factors in the recovery.

Potentially offsetting this positive evidence, we are currently in a three year cumulative loss position as of April 30, 2015. As per ASC 740, cumulative losses are one of the most objectively verifiable forms of negative evidence. Thus, an entity that has suffered cumulative losses in recent years may find it difficult to support an assertion that a DTA could be realized if such an assertion is based on forecasts of future profitable results rather than an actual return to profitability. In other words, an entity that has cumulative losses generally should not use an estimate of future earnings to support a conclusion that realization of an existing DTA is more likely than not if such a forecast is not based on objectively verifiable information. An objectively verifiable estimate of future income in that instance would be based on operating results from the reporting entity's recent history.

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We determined that the positive evidence noted above, including our two fiscal years of sustained operating profitability, outweighed the existing negative evidence and because of our current backlog, we expect to be in a three year cumulative income position by the end of fiscal 2015. Given that ASC 740 suggests using recent historical operating results in the instance where a three year cumulative loss position still exists, we used our recent historical profit levels in projecting our pretax income over the future years in assessing the utilization of our existing DTAs. Therefore, we concluded that it is more likely than not that we will realize a substantial portion of our DTAs, and that a full valuation allowance is not necessary. This analysis resulted in a partial reversal equal to $285.1 million of our valuation allowance against DTAs at October 31, 2014, leaving a remaining valuation allowance of $642.0 million at October 31, 2014. Our valuation allowance for deferred taxes amounted to $642.5 million at April 30, 2015.

17. Operating and Reporting Segments

Our operating segments are components of our business for which discrete financial information is available and reviewed regularly by the chief operating decision maker, our Chief Executive Officer, to evaluate performance and make operating decisions. Based on this criteria, each of our communities qualifies as an operating segment, and therefore, it is impractical to provide segment disclosures for this many segments. As such, we have aggregated the homebuilding operating segments into six reportable segments.

Our homebuilding operating segments are aggregated into reportable segments based primarily upon geographic proximity, similar regulatory environments, land acquisition characteristics and similar methods used to construct and sell homes. Our reportable segments consist of the following six homebuilding segments and a financial services segment:

Homebuilding:

(1) Northeast (New Jersey and Pennsylvania)

(2) Mid-Atlantic (Delaware, Maryland, Virginia, Washington D.C. and West Virginia)

(3) Midwest (Illinois, Minnesota and Ohio)

(4) Southeast (Florida, Georgia, North Carolina and South Carolina)

(5) Southwest (Arizona and Texas)

(6) West (California)

Financial Services

Operations of the Company’s Homebuilding segments primarily include the sale and construction of single-family attached and detached homes, attached townhomes and condominiums, urban infill and active adult homes in planned residential developments. In addition, from time to time, operations of the homebuilding segments include sales of land. Operations of the Company’s Financial Services segment include mortgage banking and title services provided to the homebuilding operations’ customers. We do not typically retain or service mortgages that we originate but rather sell the mortgages and related servicing rights to investors.

Corporate and unallocated primarily represents operations at our headquarters in Red Bank, New Jersey. This includes our executive offices, information services, human resources, corporate accounting, training, treasury, process redesign, internal audit, construction services, and administration of insurance, quality and safety. It also includes interest income and interest expense resulting from interest incurred that cannot be capitalized in inventory in the Homebuilding segments, as well as the gains or losses on extinguishment of debt from debt repurchases or exchanges.

Evaluation of segment performance is based primarily on operating earnings from continuing operations before provision for income taxes (“Income (loss) before income taxes”). Income (loss) before income taxes for the Homebuilding segments consist of revenues generated from the sales of homes and land, income (loss) from unconsolidated entities, management fees and other income, less the cost of homes and land sold, selling, general and administrative expenses, interest expense and non-controlling interest expense. Income before income taxes for the Financial Services segment consist of revenues generated from mortgage financing, title insurance and closing services, less the cost of such services and certain selling, general and administrative expenses incurred by the Financial Services segment.

Operational results of each segment are not necessarily indicative of the results that would have occurred had the segment been an independent stand-alone entity during the periods presented.

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Financial information relating to the Company’s segment operations was as follows:

(In thousands)	Three Months Ended April 30, 2015	2014	Six Months Ended April 30, 2015	2014
Revenues:				
Northeast	$39,274	$65,745	$90,004	$118,998
Mid-Atlantic	76,777	68,735	157,962	129,255
Midwest	73,256	48,703	137,695	92,461
Southeast	49,275	52,023	87,169	91,164
Southwest	190,427	164,633	357,614	293,210
West	27,522	40,708	60,715	71,458
Total homebuilding	456,531	440,547	891,159	796,546
Financial services	12,457	9,412	23,579	17,506
Corporate and unallocated	(39)	(30)	(75)	(75)
Total revenues	$468,949	$449,929	$914,663	$813,977
(Loss) income before income taxes:				
Northeast	$(3,812)	$(2,759)	$(6,965)	$(8,820)
Mid-Atlantic	(178)	2,462	4,999	4,375
Midwest	1,210	3,361	4,921	5,716
Southeast	(1,202)	3,315	(2,358)	4,746
Southwest	14,022	15,676	25,347	26,081
West	(8,963)	2,097	(11,336)	1,738
Homebuilding income before income taxes	1,077	24,152	14,608	33,836
Financial services	4,949	2,705	8,754	4,127
Corporate and unallocated	(35,507)	(34,155)	(72,523)	(69,151)
Loss before income taxes	$(29,481)	$(7,298)	$(49,161)	$(31,188)

(In thousands)	April 30, 2015	October 31, 2014
Assets:		
Northeast	$313,252	$315,573
Mid-Atlantic	345,473	313,494
Midwest	185,958	169,967
Southeast	202,738	148,096
Southwest	445,760	410,756
West	221,822	143,245
Total homebuilding	1,715,003	1,501,131
Financial services	127,301	120,343
Corporate and unallocated	674,690	668,456
Total assets	$2,516,994	$2,289,930

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18. Investments in Unconsolidated Homebuilding and Land Development Joint Ventures

We enter into homebuilding and land development joint ventures from time to time as a means of accessing lot positions, expanding our market opportunities, establishing strategic alliances, managing our risk profile, leveraging our capital base and enhancing returns on capital. Our homebuilding joint ventures are generally entered into with third-party investors to develop land and construct homes that are sold directly to third-party home buyers. Our land development joint ventures include those entered into with developers and other homebuilders as well as financial investors to develop finished lots for sale to the joint venture's members or other third parties.

The tables set forth below summarize the combined financial information related to our unconsolidated homebuilding and land development joint ventures that are accounted for under the equity method.

(Dollars in thousands)	April 30, 2015		
	Homebuilding	Land Development	Total
Assets:			
Cash and cash equivalents	$17,682	$122	$17,804
Inventories	306,132	14,550	320,682
Other assets	9,132	-	9,132
Total assets	$332,946	$14,672	$347,618
Liabilities and equity:			
Accounts payable and accrued liabilities	$23,428	$584	$24,012
Notes payable	91,397	4,915	96,312
Total liabilities	114,825	5,499	120,324
Equity of:			
Hovnanian Enterprises, Inc.	66,691	3,014	69,705
Others	151,430	6,159	157,589
Total equity	218,121	9,173	227,294
Total liabilities and equity	$332,946	$14,672	$347,618
Debt to capitalization ratio	30 %	35 %	30 %

(Dollars in thousands)	October 31, 2014		
	Homebuilding	Land Development	Total
Assets:			
Cash and cash equivalents	$22,415	$205	$22,620
Inventories	208,620	16,194	224,814
Other assets	11,986	-	11,986
Total assets	$243,021	$16,399	$259,420

Liabilities and equity:			
Accounts payable and accrued liabilities	$27,175	$1,039	$28,214
Notes payable	45,506	5,650	51,156
Total liabilities	72,681	6,689	79,370
Equity of:			
Hovnanian Enterprises, Inc.	59,106	2,990	62,096
Others	111,234	6,720	117,954
Total equity	170,340	9,710	180,050
Total liabilities and equity	$243,021	$16,399	$259,420
Debt to capitalization ratio	21 %	37 %	22 %

As of April 30, 2015 and October 31, 2014, we had advances outstanding of approximately $0.8 million and $1.8 million, respectively, to these unconsolidated joint ventures, which were included in the “Accounts payable and accrued liabilities” balances in the tables above. On our Condensed Consolidated Balance Sheets, our “Investments in and advances to unconsolidated joint ventures” amounted to $70.6 million and $63.9 million at April 30, 2015 and October 31, 2014, respectively.

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(In thousands)	For the Three Months Ended April 30, 2015 Homebuilding	Land Development	Total
Revenues	$27,648	$ 1,483	$29,131
Cost of sales and expenses	(29,258)	(1,722)	(30,980)
Joint venture net loss	$(1,610)	$ (239)	$(1,849)
Our share of net income (loss)	$1,465	$ (119)	$1,346

(In thousands)	For the Three Months Ended April 30, 2014 Homebuilding	Land Development	Total
Revenues	$33,746	$ 3,355	$37,101
Cost of sales and expenses	(31,644)	(3,466)	(35,110)
Joint venture net income (loss)	$2,102	$ (111)	$1,991
Our share of net income (loss)	$1,030	$ (55)	$975

(In thousands)	For the Six Months Ended April 30, 2015 Homebuilding	Land Development	Total
Revenues	$64,774	$ 2,615	$67,389
Cost of sales and expenses	(59,117)	(2,807)	(61,924)
Joint venture net income (loss)	$5,657	$ (192)	$5,465
Our share of net income (loss)	$2,932	$ (96)	$2,836

(In thousands)	For the Six Months Ended April 30, 2014 Homebuilding	Land Development	Total
Revenues	$85,019	$ 5,269	$90,288
Cost of sales and expenses	(77,725)	(5,085)	(82,810)
Joint venture net income	$7,294	$ 184	$7,478
Our share of net income	$3,577	$ 92	$3,669

“Income from unconsolidated joint ventures” is reflected as a separate line in the accompanying Condensed Consolidated Statements of Operations and reflects our proportionate share of the income or loss of these unconsolidated homebuilding and land development joint ventures. The difference between our share of the income or loss from these unconsolidated joint ventures in the tables above compared to the Condensed Consolidated Statements of Operations for the three and six months ended April 30, 2015 and 2014, is due primarily to the reclassification of the intercompany portion of management fee income from certain joint ventures and the deferral of income for lots purchased by us from certain joint ventures. To compensate us for the administrative services we provide as the manager of certain joint ventures, we receive a management fee based on a percentage of the applicable joint venture’s revenues. These management fees, which totaled $1.2 million and $1.6 million, for the three months ended April 30, 2015 and 2014, respectively, and $2.4 million and $3.7 million for the six months ended April 30, 2015 and 2014, respectively, are recorded in “Homebuilding: Selling, general and administrative” on the Condensed Consolidated Statement of Operations.

In determining whether or not we must consolidate joint ventures that we manage, we assess whether the other partners have specific rights to overcome the presumption of control by us as the manager of the joint venture. In most cases, the presumption is overcome because the joint venture agreements require that both partners agree on establishing the operations and capital decisions of the partnership, including budgets in the ordinary course of business.

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Typically, our unconsolidated joint ventures obtain separate project specific mortgage financing. The amount of financing is generally targeted to be no more than 50% of the joint venture's total assets. For some of our joint ventures, obtaining financing was challenging, therefore, some of our joint ventures are capitalized only with equity. Including the impact of impairments recorded by the joint ventures, the total debt to capitalization ratio of all our joint ventures is currently 30%. Any joint venture financing is on a nonrecourse basis, with guarantees from us limited only to performance and completion of development, environmental warranties and indemnification, standard indemnification for fraud, misrepresentation and other similar actions, including a voluntary bankruptcy filing. In some instances, the joint venture entity is considered a VIE under ASC 810-10 "Consolidation – Overall" due to the returns being capped to the equity holders; however, in these instances, we have determined that we are not the primary beneficiary, and therefore we do not consolidate these entities.

19. Recent Accounting Pronouncements

In January 2014, the Financial Accounting Standards Board ("FASB") issued Accounting Standards Update ("ASU") No. 2014-04, "Receivables - Troubled Debt Restructurings by Creditors," which clarifies when an in substance repossession or foreclosure of residential real estate property collateralizing a consumer mortgage loan has occurred. By doing so, this guidance helps determine when the creditor should derecognize the loan receivable and recognize the real estate property. The guidance is effective for the Company beginning November 1, 2015 and is not expected to have a material impact on the Company's Condensed Consolidated Financial Statements.

In May 2014, the FASB issued Accounting Standards Update ("ASU") No. 2014-09, "Revenue from Contracts with Customers" (Topic 606), ("ASU 2014-09"). ASU 2014-09 requires entities to recognize revenue that represents the transfer of promised goods or services to customers in an amount equivalent to the consideration to which the entity expects to be entitled to in exchange for those goods or services. The following steps should be applied to determine this amount: (1) identify the contract(s) with a customer; (2) identify the performance obligations in the contract; (3) determine the transaction price; (4) allocate the transaction price to the performance obligations in the contract; and (5) recognize revenue when (or as) the entity satisfies a performance obligation. ASU 2014-09 supersedes the revenue recognition requirements in ASU 605, "Revenue Recognition", and most industry-specific guidance in the Accounting Standards Codification. The FASB has tentatively decided to defer for one year the effective date of ASU 2014-09, which would make the guidance effective for the Company beginning November 1, 2018. Additionally, the FASB also tentatively decided to permit entities to early adopt the standard, which allows for either full retrospective or modified retrospective methods of adoption, for reporting periods beginning after December 15, 2016. We are currently evaluating the impact of adopting this guidance on our Condensed Consolidated Financial Statements.

In June 2014, the FASB issued ASU 2014-11, "Repurchase-to-Maturity Transactions, Repurchase Financings, and Disclosures" ("ASU 2014-11"), which makes limited amendments to ASC 860, "Transfers and Servicing." ASU 2014-11 requires entities to account for repurchase-to-maturity transactions as secured borrowings, eliminates accounting guidance on linked repurchase financing transactions, and expands disclosure requirements related to certain transfers of financial assets. ASU 2014-11 was effective for the Company beginning February 1, 2015, and did not have a material impact on the Company's Condensed Consolidated Financial Statements.

In August 2014, the FASB issued ASU 2014-15, “Disclosure of Uncertainties About an Entity’s Ability to Continue as a Going Concern” (“ASU 2014-15”), which requires management to perform interim and annual assessments on whether there are conditions or events that raise substantial doubt about the entity’s ability to continue as a going concern within one year of the date the financial statements are issued and to provide related disclosures, if required. ASU 2014-15 is effective for the Company for our fiscal year ending October 31, 2017. Early adoption is permitted. We do not anticipate the adoption of ASU 2014-15 to have a material impact on the Company’s Condensed Consolidated Financial Statements.

In February 2015, the FASB issued ASU 2015-02, “Consolidation (Topic 810): Amendments to the Consolidation Analysis (“ASU 2015-02”), which amends the consolidation requirements in ASC 810, primarily related to limited partnerships and VIEs. ASU 2015-02 is effective for the Company beginning on November 1, 2016. Early adoption is permitted. We do not anticipate the adoption of ASU 2015-02 to have a material impact on the Company’s Condensed Consolidated Financial Statements.

In April 2015, the FASB issued ASU 2015-03, “Interest - Imputation of Interest” (“ASU 2015-03”), which requires that debt issuance costs related to a recognized debt liability be presented in the balance sheet as a direct deduction from the carrying amount of that debt liability. This new guidance is a change from the current treatment of recording debt issuance costs as an asset representing a deferred charge, and is consistent with the accounting treatment for debt discounts. The guidance, which requires retrospective application, is effective for the Company beginning November 1, 2016. Early adoption is permitted. We do not anticipate the adoption of ASU 2015-03 to have a material impact on the Company’s Condensed Consolidated Financial Statements.

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20. Fair Value of Financial Instruments

ASC 820, "Fair Value Measurements and Disclosures," provides a framework for measuring fair value, expands disclosures about fair-value measurements and establishes a fair-value hierarchy which prioritizes the inputs used in measuring fair value summarized as follows:

Level 1:	Fair value determined based on quoted prices in active markets for identical assets.
Level 2:	Fair value determined using significant other observable inputs.
Level 3:	Fair value determined using significant unobservable inputs.

Our financial instruments measured at fair value on a recurring basis are summarized below:

(In thousands)	Fair Value Hierarchy	Fair Value at April 30, 2015	Fair Value at October 31, 2014
Mortgage loans held for sale (1)	Level 2	$106,318	$95,643
Interest rate lock commitments	Level 2	(44)	15
Forward contracts	Level 2	178	(320)
		$106,452	$95,338

(1) The aggregate unpaid principal balance was $100.9 million and $91.2 million at April 30, 2015 and October 31, 2014, respectively.

We elected the fair value option for our loans held for sale for mortgage loans originated subsequent to October 31, 2008, in accordance with ASC 825, "Financial Instruments," which permits us to measure financial instruments at fair value on a contract-by-contract basis. Management believes that the election of the fair value option for loans held for sale improves financial reporting by mitigating volatility in reported earnings caused by measuring the fair value of the loans and the derivative instruments used to economically hedge them without having to apply complex hedge accounting provisions. Fair value of loans held for sale is based on independent quote market prices, where available, or the prices for other mortgage whole loans with similar characteristics.

The Financial Services segment had a pipeline of loan applications in process of $630.6 million at April 30, 2015. Loans in process for which interest rates were committed to the borrowers totaled approximately $53.9 million as of April 30, 2015. Substantially all of these commitments were for periods of 60 days or less. Since a portion of these commitments is expected to expire without being exercised by the borrowers, the total commitments do not necessarily represent future cash requirements.

The Financial Services segment uses investor commitments and forward sales of mandatory MBS to hedge its mortgage-related interest rate exposure. These instruments involve, to varying degrees, elements of credit and interest rate risk. Credit risk is managed by entering into MBS forward commitments, option contracts with investment banks, federally regulated bank affiliates and loan sales transactions with permanent investors meeting the segment's credit standards. The segment's risk, in the event of default by the purchaser, is the difference between the contract price and fair value of the MBS forward commitments and option contracts. At April 30, 2015, the segment had open commitments amounting to $19.5 million to sell MBS with varying settlement dates through May 20, 2015.

The assets accounted for using the fair value option are initially measured at fair value. Gains and losses from initial measurement and subsequent changes in fair value are recognized in the Financial Services segment's income. The changes in fair values that are included in income are shown, by financial instrument and financial statement line item, below:

	Three Months Ended April 30, 2015		
(In thousands)	Mortgage Loans Held For Sale	Interest Rate Lock Commitments	Forward Contracts
Changes in fair value included in net loss all reflected in financial services revenues	$(233)	$(325)	$880

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(In thousands)	Three Months Ended April 30, 2014 Mortgage Loans Held For Sale		Interest Rate Lock Commitments		Forward Contracts
Changes in fair value included in net loss all reflected in financial services revenues	$(465	)	$(78	)	$599

(In thousands)	Six Months Ended April 30, 2015 Mortgage Loans Held For Sale		Interest Rate Lock Commitments		Forward Contracts
Changes in fair value included in net loss all reflected in financial services revenues	$(173	)	$(59	)	$498

(In thousands)	Six Months Ended April 30, 2014 Mortgage Loans Held For Sale		Interest Rate Lock Commitments		Forward Contracts
Changes in fair value included in net loss all reflected in financial services revenues	$(1,889	)	$(198	)	$686

The Company’s assets measured at fair value on a nonrecurring basis are those assets for which the Company has recorded valuation adjustments and write-offs during the periods presented. The assets measured at fair value on a nonrecurring basis are all within the Company’s Homebuilding operations and are summarized below:

Nonfinancial Assets

(In thousands)	Fair Value	Three Months Ended April 30, 2015

	Hierarchy	Pre-Impairment Amount	Total Losses	Fair Value
Sold and unsold homes and lots under development	Level 3	$11,055	$(3,543)	$7,512
Land and land options held for future development or sale	Level 3	$-	$-	$-

(In thousands)	Fair Value Hierarchy	Three Months Ended April 30, 2014 Pre-Impairment Amount	Total Losses	Fair Value
Sold and unsold homes and lots under development	Level 3	$-	$-	$-
Land and land options held for future development or sale	Level 3	$236	$(82)	$154

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(In thousands)	Fair Value Hierarchy	Six Months Ended April 30, 2015 Pre-Impairment Amount	Total Losses	Fair Value
Sold and unsold homes and lots under development	Level 3	$16,756	$(4,466)	$12,290
Land and land options held for future development or sale	Level 3	$-	$-	$-

(In thousands)	Fair Value Hierarchy	Six Months Ended April 30, 2014 Pre-Impairment Amount	Total Losses	Fair Value
Sold and unsold homes and lots under development	Level 3	$-	$-	$-
Land and land options held for future development or sale	Level 3	$236	$(82)	$154

We record impairment losses on inventories related to communities under development and held for future development when events and circumstances indicate that they may be impaired and the undiscounted cash flows estimated to be generated by those assets are less than their related carrying amounts. If the expected undiscounted cash flows are less than the carrying amount, then the community is written down to its fair value. We estimate the fair value of each impaired community by determining the present value of its estimated future cash flows at a discount rate commensurate with the risk of the respective community. Should the estimates or expectations used in determining cash flows or fair value decrease or differ from current estimates in the future, we may be required to recognize additional impairments. We recorded inventory impairments, which are included in the Condensed Consolidated Statements of Operations as “Inventory impairment loss and land option write-offs” and deducted from inventory, of $3.5 million and $4.4 million for the three and six months ended April 30, 2015, respectively, and $0.1 million for both the three and six months ended April 30, 2014.

The fair value of our cash equivalents and restricted cash approximates their carrying amount, based on Level 1 inputs.

The fair value of each series of the senior unsecured notes (other than the 7.0% Senior Notes due 2019, (the “2019 Notes”) the senior exchangeable notes and the senior amortizing notes) is estimated based on recent trades or quoted market prices for the same issues or based on recent trades or quoted market prices for our debt of similar security and maturity to achieve comparable yields, which are Level 2 measurements. The fair value of the senior unsecured notes (all series in the aggregate), other than the 2019 Notes, senior exchangeable notes and senior amortizing notes, was estimated at $701.1 million and $464.4 million as of April 30, 2015 and October 31, 2014, respectively.

The fair value of each of the 2019 Notes, the senior secured notes (all series in the aggregate), the senior amortizing notes and the senior exchangeable notes is estimated based on third party broker quotes, a Level 3 measurement. The fair value of the 2019 Notes, senior secured notes (all series in the aggregate), the senior amortizing notes and the senior exchangeable notes was estimated at $143.3 million, $993.0 million, $15.0 million and $77.8 million, respectively, as of April 30, 2015. As of October 31, 2014, the fair value of the 2019 Notes, senior secured notes (all series in the aggregate), senior amortizing notes and senior exchangeable notes was estimated at $148.2 million, $1.0 billion, $17.0 million and $79.6 million, respectively.

21. Financial Information of Subsidiary Issuer and Subsidiary Guarantors

Hovnanian Enterprises, Inc., the parent company (the “Parent”), is the issuer of publicly traded common stock and preferred stock, which is represented by depository shares. One of its wholly owned subsidiaries, K. Hovnanian Enterprises, Inc. (the “Subsidiary Issuer”), acts as a finance entity that, as of April 30, 2015, had issued and outstanding approximately $992.0 million of senior secured notes ($980.6 million, net of discount), $841.1 million senior notes ($840.9 million, net of discount) and $15.0 million senior amortizing notes and $71.9 million senior exchangeable notes (issued as components of our 6.0% Exchangeable Note Units). The senior secured notes, senior notes, senior amortizing notes and senior exchangeable notes are fully and unconditionally guaranteed by the Parent.

In addition to the Parent, each of the wholly owned subsidiaries of the Parent other than the Subsidiary Issuer (collectively, “Guarantor Subsidiaries”), with the exception of our home mortgage subsidiaries, certain of our title insurance subsidiaries, joint ventures, subsidiaries holding interests in our joint ventures and our foreign subsidiary (collectively, the “Nonguarantor Subsidiaries”), have guaranteed fully and unconditionally, on a joint and several basis, the obligations of the Subsidiary Issuer to pay principal and interest under the senior secured notes (other than the 2021 Notes), senior notes, senior exchangeable notes and senior amortizing notes. The Guarantor Subsidiaries are directly or indirectly 100% owned subsidiaries of the Parent. The 2021 Notes are guaranteed by the Guarantor Subsidiaries and the members of the Secured Group (see Note 11).

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The senior unsecured notes (except for the 2019 Notes), senior amortizing notes and senior exchangeable notes have been registered under the Securities Act of 1933, as amended. The 2019 Notes, 2020 Secured Notes and the 2021 Notes (see Note 11) are not, pursuant to the indentures under which such notes were issued, required to be registered. The Condensed Consolidating Financial Statements presented below are in respect of our registered notes only and not the 2019 Notes, 2020 Secured Notes or the 2021 Notes (however, the Guarantor Subsidiaries for the 2019 Notes and the 2020 Secured Notes are the same as those represented by the accompanying Condensed Consolidating Financial Statements). In lieu of providing separate financial statements for the Guarantor Subsidiaries of our registered notes, we have included the accompanying Condensed Consolidating Financial Statements. Therefore, separate financial statements and other disclosures concerning such Guarantor Subsidiaries are not presented.

The following Condensed Consolidating Financial Statements present the results of operations, financial position and cash flows of (i) the Parent, (ii) the Subsidiary Issuer, (iii) the Guarantor Subsidiaries, (iv) the Nonguarantor Subsidiaries and (v) the eliminations to arrive at the information for Hovnanian Enterprises, Inc. on a consolidated basis.

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HOVNANIAN ENTERPRISES, INC. AND SUBSIDIARIES

NOTES TO CONDENSED CONSOLIDATED FINANCIAL STATEMENTS

CONDENSED CONSOLIDATING BALANCE SHEET

APRIL 30, 2015

(In Thousands)

	Parent	Subsidiary Issuer	Guarantor Subsidiaries	Nonguarantor Subsidiaries	Eliminations	Consolidated
ASSETS:						
Homebuilding	$-	$247,616	$1,478,889	$362,600	$-	$2,089,105
Financial services			10,327	116,974		127,301
Income taxes receivable	258,121		42,467			300,588
Intercompany receivable		1,467,671		36,727	(1,504,398)	-
Investments in and amounts due from consolidated subsidiaries			365,247		(365,247)	-
Total assets	$258,121	$1,715,287	$1,896,930	$516,301	(1,869,645)	$2,516,994
LIABILITIES AND EQUITY:						
Homebuilding	$3,183	$196	$550,981	$55,853		$610,213
Financial services			10,021	94,776		104,797
Notes payable		1,946,342	1,551	425		1,948,318
Intercompany payable	305,378		1,199,020		(1,504,398)	-
Amounts due to consolidated subsidiaries	95,894					